COMMONWEALTH OF VIRGINIA

STATE CORPORATION COMMISSION

AT RICHMOND, NOVEMBER 10, 2004

COMMONWEALTH OF VIRGINIA, ex rel.

STATE CORPORATION COMMISSION CASE NO. PUE-2000-00551

Ex Parte: In the matter concerning the
application of Virginia Electric and Power
Company d/b/a Dominion Virginia Power
for approval of a plan to transfer functional and
operational control of certain transmission
facilities to a regional transmission entity

ORDER GRANTING APPROVAL

On June 27, 2003, Virginia Electric and Power Company d/b/a Dominion Virginia Power ("DVP," "Virginia Power," or "Company") filed with the State Corporation Commission ("Commission") an amended application ("Application") requesting approval to transfer functional and operational control of its transmission facilities to a regional transmission entity ("RTE").

Sections 56-577 and 56-579 of the Virginia Electric Utility Restructuring Act ("Restructuring Act"), Chapter 23 (§ 56-576 et seq.) of Title 56 of the Code of Virginia ("Code"), require Virginia's incumbent electric utilities to file applications with, and to seek approval from, the Commission to transfer the management and control of their transmission assets to an RTE.

Section 56-579 A 1 of the Restructuring Act was amended by the 2003 General Assembly to delay transfers to RTEs until July 1, 2004, and to require such transfers by January 1, 2005, subject to Commission approval. Section 56-579 A 1, as amended, provides in pertinent part:

> No such incumbent electric utility shall transfer to any person any ownership or control of, or any responsibility to operate, any portion of any transmission system located in the Commonwealth

> prior to July 1, 2004, and without obtaining, following notice and hearing, the prior approval of the Commission, as hereinafter provided. However, each incumbent electric utility shall file an application for approval pursuant to this section by July 1, 2003, and shall transfer management and control of its transmission assets to a regional transmission entity by January 1, 2005, subject to Commission approval as provided in this section.

In addition, § 56-579 F of the Restructuring Act was amended by the 2003 General Assembly with the addition of the following:

> Any request to the Commission for approval of such transfer of ownership or control of or responsibility for transmission facilities shall include a study of the comparative costs and benefits thereof, which study shall analyze the economic effects of the transfer on consumers, including the effects of transmission congestion costs. The Commission may approve such a transfer if it finds, after notice and hearing, that the transfer satisfies the conditions contained in this section.

Pursuant to § 56-579 A 2 of the Restructuring Act, the Commission developed and established rules and regulations under which incumbent utilities owning, operating, controlling, or having an entitlement to transmission capacity within the Commonwealth may transfer all or part of such control, ownership, or responsibility to an RTE, 20 VAC 5-320-10 et seq. ("RTE Rules").[1] The RTE Rules establish elements of an RTE structure essential to the public interest, which are to be considered by the Commission in determining whether to authorize transfer of control of incumbent electric utilities' transmission assets to an RTE. The RTE Rules require the examination of, among other things, an RTE's reliability practices, pricing and access policies, and independent governance. The Application, therefore, must be considered pursuant to the directives set forth in the Restructuring Act and must comply with the RTE Rules.

[1] Commonwealth of Virginia, ex rel. State Corporation Commission, Ex Parte: In the matter concerning participation of incumbent electric utilities in regional transmission entities, Case No. PUE-1999-00349, 2000 S.C.C. Ann. Rept. 430.

Virginia Power now seeks approval of the transfer of control of its transmission facilities to PJM Interconnection, LLC ("PJM"), an existing regional transmission organization ("RTO")[2] with day-ahead and real-time markets for energy[3] and ancillary services. The history of this proceeding is extensive. The Company filed with the Commission its original application to join an RTE on October 16, 2000. Since DVP's original application was filed with the Commission, numerous significant events have occurred at both the state and federal level. These events resulted in delays in the approval of the transfer of control of the transmission systems of both DVP and Appalachian Power Company d/b/a American Electric Power-Virginia ("AEP-VA") to an RTE.

The Company's original application sought approval from this Commission to transfer the operational and functional control of its transmission facilities to the Alliance RTO, an RTO that was to be created pursuant to federal regulations issued by the Federal Energy Regulatory Commission ("FERC").[4] The FERC issued a number of rulings in the Alliance RTO proceedings. On July 27, 2001, this Commission by order suspended the original procedural schedule based on anticipated filings by the Alliance Companies at the FERC. After over two years of consideration by our federal counterpart, including several initial rulings conditionally

[2] The phrases Regional Transmission Entity or RTE and Regional Transmission Organization or RTO may be used interchangeably.

[3] PJM's energy market, which also serves as the basis for PJM's congestion management system, utilizes Locational Marginal Pricing ("LMP").

[4] Alliance Companies, et al., Docket Nos. ER99-3144-003, ER99-3144-004 and ER99-3144-005. The proposed Alliance RTO was to consist of the following member companies: American Electric Power Service Corporation; Consumers Energy Company; Commonwealth Edison Company ("ComEd"); The Dayton Power and Light Company ("Dayton Power"); The Detroit Edison Company; FirstEnergy Corp. on behalf of the Cleveland Electric Illuminating Company, Ohio Edison Company, Pennsylvania Power Company, and the Toledo Edison Company; the Northern Indiana Public Service Company; and Virginia Power (collectively the "Alliance Companies"). The proposed Alliance RTO was to include incumbent electric utilities who provide service in the states of Illinois, Indiana, Kentucky, Michigan, Missouri, Ohio, Pennsylvania, North Carolina, Tennessee, Virginia, and West Virginia.

approving the Alliance RTO, the FERC disapproved the Alliance RTO on December 20, 2001, and dismissed in whole the Alliance Companies' proposal.[5] On January 29, 2002, because of the FERC's ruling that dismissed the Alliance RTO proposal, this Commission issued an order denying a motion to reestablish a procedural schedule in Virginia Power's and AEP-VA's RTE dockets.

On April 25, 2002, the FERC issued an order directing the Alliance Companies to make compliance filings identifying which RTO they planned to join and stating whether their participation would be collective or individual.[6] On May 28, 2002, DVP made its compliance filing with the FERC. In its filing, the Company explained that it had filed a statement with the FERC on March 5, 2002, indicating that it was continuing the process of consulting with this Commonwealth and the State of North Carolina to determine their support for DVP joining the Alliance Companies within the Midwest Independent System Operator, or for other RTO efforts. DVP further stated that the Company also was actively working with PJM, on an individual basis, as well as collectively with the Alliance Companies. Subsequently, DVP and PJM entered into a Memorandum of Understanding dated June 24, 2002, to establish PJM South.

On July 31, 2002, the FERC issued a notice of proposed rulemaking to establish a national Standard Market Design ("SMD") for wholesale electricity markets ("SMD NOPR").[7]

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[5] Alliance Companies, et al., 97 FERC ¶ 61,327 (2001). In its Order dismissing the Alliance Companies' application, the FERC found that the proposed Alliance did not comply with key requirements of the FERC's Order No. 2000.

[6] Alliance Companies, et al., 99 FERC ¶ 61,105 (2002).

[7] Remedying Undue Discrimination Through Open Access Transmission Service and Standard Electricity Market Design, Notice of Proposed Rulemaking, 67 Fed. Reg. 55452 (2002) (to be codified at 18 C.F.R. pt. 35) (proposed July 31, 2002). Virginia Code § 56-579 C provides that the Commission, to the fullest extent permitted under federal law, shall participate in FERC proceedings concerning RTEs. On January 31, 2003, this Commission filed comments on the SMD NOPR.

The SMD NOPR requires, among other things, all public utilities to turn over the operation of their transmission facilities to an Independent Transmission Provider ("ITP").[8]

On October 1, 2002, the Company and PJM entered into an agreement to implement PJM South. On December 10, 2002, DVP filed with the FERC a rate reciprocity agreement under which DVP sought to charge rates to its transmission customers as if DVP were already a PJM member ("DVP RRA Filing").[9] On December 11, 2002, DVP in conjunction with ComEd, Dayton Power, American Electric Power Corporation ("AEP"), and PJM, filed a request with the FERC asking that certain companies be allowed to participate in PJM as transmission owners ("PJM Expansion Proceeding").[10] The request further asked that PJM's transmission owners' agreements, Operating Agreement, and Open Access Transmission Tariff be modified accordingly.[11] On December 20, 2002, the FERC issued a ruling on PJM's application for RTO status, granting PJM full RTO status subject to the satisfaction of certain conditions.[12]

On January 7, 2003, DVP filed a Motion to Dismiss its application in this docket to transfer functional and operational control of its transmission assets to the Alliance RTO. In our order issued February 5, 2003, the Commission dismissed DVP's application to join the Alliance, but ordered that the docket remain open to receive a future RTE application from the Company.

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[8] The SMD NOPR would require all public utilities that own, control, or operate facilities used for the transmission of electric energy in interstate commerce to: (1) meet the definition of an ITP itself; (2) turn over the operation of its transmission facilities to an RTO that is an ITP; or (3) contract with an ITP to operate the utility's transmission facilities. The FERC stated it expects that most, if not all, public utilities will become members of RTOs.

[9] Virginia Electric and Power Company, Docket No. ER03-242-000.

[10] New PJM Companies and PJM Interconnection, L.L.C., Docket Nos. ER03-262-000 and ER03-262-001. Virginia Power did not seek to participate in PJM as a transmission owner in the December 11, 2002, filing. AEP, Commonwealth Edison, and Dayton Power sought approval to participate in PJM as transmission owners.

[11] The Commission filed comments in both the DVP RRA filing and the PJM Expansion Proceeding.

[12] PJM Interconnection, L.L.C., et al., Docket Nos. RT01-2-001, RT01-2-002, 101 FERC ¶ 61,345 (2002).

On April 1, 2003, the FERC rejected DVP's RRA Filing, finding that rate adjustments to ensure revenue neutrality were unreasonable in the current circumstance where DVP would not be transferring operational control of its transmission facilities until some time in the future.[13] On April 28, 2003, the FERC issued its White Paper in the SMD NOPR proceeding.[14] In its White Paper, the FERC attempted to address concerns articulated by some state and regional entities protesting the SMD NOPR, but advocated, among other things, mandatory RTO participation by all public utilities.

On September 26, 2003, the Commission issued an Order for Notice ("September 26 Order") in this proceeding that, among other things: (1) directed the Company to provide notice to the public of its Application; (2) provided the opportunity for interested persons not already participating in the proceeding to participate; (3) directed the Company to file additional cost/benefit information; and (4) directed the Company to file certain additional information after the FERC issued a final rule in its SMD NOPR. The September 26 Order stated that the Commission could not fully consider the Application and make a final determination on its merits until the FERC issued a final SMD rule and until that rule's impact on PJM's operations could be evaluated. The Commission explained that any final SMD rule could directly affect the structure and operations of PJM, and that the SMD NOPR asserts expansive jurisdiction over both the transmission and generation of electricity. Thus, the September 26 Order concluded that the SMD NOPR has far-reaching jurisdictional implications and the potential to alter profoundly the nature of electricity regulation on the federal and state levels.

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[13] Virginia Electric and Power Company, Docket No. ER03-257-000, 103 FERC ¶ 61,010 (2003).

[14] Remedying Undue Discrimination Through Open Access Transmission Service and Standard Electricity Market Design, Notice of Proposed Rulemaking, Notice of White Paper issued April 28, 2003.

On December 22, 2003, the Commission issued an Order on Motion for Modification ("December 22 Order") that, among other things: (1) denied DVP's request to eliminate certain informational requirements directed by the September 26 Order; (2) granted DVP an extension by which to file such additional information from November 26, 2003, to February 1, 2004; (3) granted the Company's motion not to delay this proceeding pending a final SMD; and (4) established the remaining procedural schedule for this matter. The December 22 Order concluded that changed circumstances made it appropriate to revise the September 26 Order. Specifically, the December 22 Order noted that the United States Congress released a draft Conference Report on the Energy Policy Act of 2003, which would have prohibited any SMD rule from taking effect before December 31, 2006. Thus, in light of the prospects that FERC may be prevented by federal law from implementing final SMD rules until January 2007, and that FERC may not proceed with its SMD NOPR in any event, we granted the Company's request that the absence of final SMD rules not delay consideration of its Application. On January 22, 2004, the Commission issued an Order granting the Company's request to further extend the date for filing its additional information from February 1, 2004, to March 15, 2004.

On March 15, 2004, Virginia Power filed: (1) a Compliance Report on the additional information required by the September 26 Order; (2) supplemental direct testimony of William L. Thompson, Director/ Electric Transmission Systems Operations Center; (3) supplemental direct testimony of Ronnie Bailey, Manager – Electric Transmission Planning; (4) supplemental direct testimony of David F. Koogler, Director – Regulation and Competition; and (5) supplemental direct testimony of Robert Stoddard, Vice President in the Energy and Environment practice at Charles River Associates Incorporated. Mr. Thompson testifies that the Northeast Blackout of August 14, 2003, amplifies the strengths to be gained from a reliability

perspective if the Company joins PJM. Mr. Bailey also testifies that the August 14, 2003, blackout strengthens DVP's reasons for joining PJM because, among other things, the blackout demonstrates the need for improved regional planning. Mr. Koogler provides updated information on transmission rates and explains that the integration of AEP and DVP into PJM will eliminate the need for competitive service providers to secure specific firm transmission paths from AEP or existing PJM members to gain entry into the Company's transmission zone. Mr. Stoddard discusses cost and reliability impacts of centralized dispatch based on LMP, presents a sensitivity case to the Company's cost/benefit study reflecting PJM's current operation of a key transmission line, and makes three corrections to the Company's cost/benefit study.

On May 11, 2004, as amended on July 6, 2004, Virginia Power and PJM submitted for approval by the FERC, pursuant to Section 205 of the Federal Power Act ("FPA"), 16 U.S.C. § 824d, their joint proposal to establish PJM South.[15]

On June 25, 2004, the Company filed in the instant case a Supplemental Report updating its cost/benefit study to reflect Senate Bill No. 651, which was passed by the 2004 General Assembly. Specifically, the Supplemental Report reflects: (1) freezing the fuel factor at its current level until July 1, 2007; (2) including a one-time adjustment to the fuel factor for the period July 1, 2007, to December 31, 2010; and (3) continuing capped rates through December 31, 2010. The Supplemental Report provides a High End Quantitative Benefit Case ("high end case") and a Low End Quantitative Benefit Case ("low end case") for the study period of January 1, 2005, through December 31, 2014. The high end case assumes that, on July 1, 2007, all of DVP's retail customers choose an alternative supplier and leave capped rates. Under the high end case, the present value of quantitative net benefits to Virginia retail customers is

[15] PJM Interconnection, L.L.C., and Virginia Electric and Power Company, Docket Nos. ER04-829-000 and ER04-829-001 ("PJM South").

$463.5 million over the ten-year study period. The low end case assumes that all of DVP's retail customers remain on capped rates until December 31, 2010. Under the low end case, the present value of quantitative net benefits to Virginia retail customers is $255 million over the ten-year study period.

On July 15, 2004, the Division of Consumer Counsel of the Office of the Attorney General ("Consumer Counsel") filed the direct testimony of Seth W. Brown, Principal and the Manager of Transmission Services at GDS Associates. Mr. Brown states that Consumer Counsel supports Commission approval of DVP's application to transfer functional control of its transmission facilities to PJM. However, Mr. Brown testifies that Commission approval should be conditioned upon any combination of mechanisms available to assure that the qualitative and quantitative net benefits identified by DVP are equitably shared with Virginia ratepayers. Mr. Brown contends that such potential mechanisms include:

1. Consistent with DVP's representations in its Application and the applicable PJM procedures, DVP should be required to select a "hold harmless" portfolio of financial transmission rights ("FTRs") so as to minimize any "unhedgable congestion" associated with deliveries from its generation and its economic purchases to its network and native load. To the extent that DVP selects FTRs from its generation to hedge potential economic off-system sales, the amount of FTRs available to hedge against congestion costs for DVP's network and native load obligations should not be reduced.

2. Consistent with DVP's representation in its Application and the applicable PJM procedures, DVP should be required to maintain a single "load aggregation zone" for congestion pricing purposes.

3. Consistent with DVP's representation in its Application, approval should be conditioned on PJM's commitment not to shed load in the DVP Zone to address generating capacity deficiencies that might arise in other areas of PJM.

4. Approval of DVP's Application should be conditioned on DVP maintaining its current transmission charge as its zonal license

plate charge in PJM in order to realize the net benefits quantified in the Company's cost/benefit study.

5. As DVP did not factor into its cost benefit analyses any deferred RTO integration and development costs, if the Company does not supplement its application to incorporate these costs, DVP should be denied recovery of such costs.

6. Because DVP did not factor into its cost/benefit analyses any FERC return-on-equity incentives for joining a FERC-approved RTO, if DVP does not supplement its application to incorporate these costs, DVP should be denied recovery from Virginia ratepayers of any increases in transmission rates due to such FERC incentives.

7. Any conditions should be considered that reasonably flow from the Company's cost/benefit study, which categorizes DVP's PJM administrative costs as both a charge against shareholder benefits during the capped rate period and as a regulatory asset to be collected from ratepayers after the capped rate period.

On July 15, 2004, the Virginia Committee for Fair Utility Rates ("Committee") filed the direct testimony of Burnice C. Dooley, a partner in the firm of Dooley & Vicars, CPAs, LLP. Mr. Dooley states that DVP's cost/benefit study assumes PJM administrative charges are deferred through 2010 and recovered over the balance of the study period. As a result, the Company's cost/benefit study assigns no PJM administrative charges to the period from 2005 through 2010; instead, all PJM administrative charges, including those incurred from 2005 through 2010, are assigned to the period after 2010. Mr. Dooley concludes that under this assumption, DVP's customers are, in effect, accruing a liability to pay for the PJM administrative charges. Mr. Dooley states that if the cost/benefit study had reflected the annual effect of this accrued liability through 2010, net customer benefits would disappear in the low end case (and result in net customer costs) but there would still be considerable benefits in the high end case. Mr. Dooley explains that DVP has sought FERC approval to defer recognition of PJM administrative charges for accounting purposes until after the expiration of the capped rate

period (i.e., December 31, 2010), and that DVP will later seek recovery of such costs through a rate filing with FERC. Mr. Dooley testifies that if FERC grants both requests, the Company could flow such charges to Virginia retail customers after the expiration of capped rates. Mr. Dooley also notes that Virginia Power is not requesting a similar cost deferral for its retail customers in North Carolina. Mr. Dooley recommends that the Commission condition any approval in this case on DVP agreeing not to seek to defer PJM administrative charges for retail ratemaking purposes. Mr. Dooley asserts that this would be consistent with Virginia Power's statements during the recent General Assembly Session that the Restructuring Act – and in particular, capped rates – shifts risks for cost increases from Virginia Power's customers to its shareholders. Mr. Dooley concludes that deferring the PJM administrative charges until after the expiration of capped rates imposes the risk of such cost increases on customers, not on shareholders.

On July 15, 2004, Coral Power, L.L.C. ("Coral"), filed the direct testimony of James J. Cifaratta, Vice President – Assets for Shell Trading Gas & Power. Mr. Cifaratta's responsibilities include managing Coral's Energy Conversion Agreement ("ECA") with Tenaska Virginia Partners, L.P. ("Tenaska"). The ECA is associated with Tenaska's 885 MW natural gas fired, combined cycle generating facility in Fluvanna County ("Fluvanna Facility"). Mr. Cifaratta addresses Coral's support for DVP's Application to join PJM. Mr. Cifaratta discusses the important role that PJM's independence plays in developing and enhancing confidence in the region's electricity markets. Mr. Cifaratta identifies his concerns with the impacts resulting from any delay in the participation by DVP in PJM's markets. Finally, Mr. Cifaratta describes the additional reliability and economic benefits that full participation in the markets administered by PJM can provide to consumers in the Virginia region, and he

discusses how Coral can enhance those benefits through its participation in the region's wholesale electric markets with the Fluvanna Facility.

On August 16, 2004, the Commission's Staff ("Staff") filed the direct testimony of Cody D. Walker, an Assistant Director in the Commission's Division of Energy Regulation. Mr. Walker's testimony: (1) provides an overview of PJM; (2) discusses whether the Company's Application satisfies the Commission's RTE Rules; (3) discusses whether DVP has any alternatives to joining PJM; (4) discusses the implications of the Company's integration into PJM; and (5) discusses the costs and benefits of DVP's participation in PJM. Mr. Walker states that the Company's request to join PJM sufficiently satisfies the RTE Rules provided that the Company can secure FERC approval of its application to form PJM South. Mr. Walker asserts that the Company's integration into PJM may have certain negative implications with respect to reliability and that the Staff has reservations about the effectiveness of market monitoring in general. However, Mr. Walker concludes that PJM represents one of the best, if not the best, available RTO models. In addition, Mr. Walker testifies that the Staff engaged Henwood Energy Services, Inc. ("Henwood"), to provide an independent assessment of the costs and benefits of the Company's and AEP-VA's proposed integration into PJM. Mr. Walker explains that Henwood's assessment finds that the Company's participation in a fully expanded PJM, when viewed from an overall net present value perspective, will produce very slight positive results of 0% to 1% of the total costs of serving load. Mr. Walker further explained during the evidentiary hearing that the Henwood analysis shows that the impact on ratepayers would range from a negative impact of $85 million to a positive impact of $62.2 million if DVP is ultimately allowed to recover deferred PJM administrative charges from ratepayers.

In addition, Mr. Walker testifies that, under the Restructuring Act, the public policy of the Commonwealth is that Virginia utilities should transfer functional control of transmission systems to RTEs, and that PJM appears to be the only feasible option that can satisfy the January 1, 2005, statutory target established in the Restructuring Act. Thus, if the Commission determines that the Company should satisfy the Restructuring Act through integration into PJM, Mr. Walker recommends that DVP's Application be approved with specific conditions attached to such approval. Mr. Walker lists potential conditions for the Commission's consideration, which address: (1) certain reporting requirements for DVP; (2) modification of PJM's curtailment protocols in order to protect native retail load; (3) retention of the Commission's jurisdiction over any subsequent transfer of operation and control of the Company's transmission facilities by DVP or any other operator; and (4) DVP obtaining FERC approval of its participation in PJM and complying with any conditions associated with such approval.

On August 16, 2004, the Staff filed the direct testimony of Mark R. Griffith, a Vice President in the Strategic Consulting and Advisory Services business unit at Henwood. Mr. Griffith analyzes the costs and benefits associated with the Company's Application to join PJM. Mr. Griffith sponsors the Staff's cost/benefit study, which is referenced by Mr. Walker. Mr. Griffith explains how he approached his analysis and presents a summary of his findings.

On August 16, 2004, the Staff also filed the direct testimony of Howard M. Spinner, the Director of the Commission's Division of Economics and Finance. Mr. Spinner addresses key issues surrounding LMP for electric energy as practiced in the energy markets administered by PJM. Mr. Spinner asserts that there are problems with PJM's LMP model as a means for allocating scarce electrical resources and that there are questions as to the ability of PJM's market monitoring unit to ensure good results. Mr. Spinner also testifies that the reliability implications

of the Company's Application appear not to be a decisive factor. Mr. Spinner concludes that, realizing that the Company's integration into PJM at this time will assist it in satisfying the January 1, 2005, legislative target for RTE integration established by the Restructuring Act, and also recognizing that DVP's generating units remain legally connected to the Company's Virginia retail customers, he believes that the Commission could conclude that the Company's Application is in the public interest.

On September 17, 2004, the Company filed the rebuttal testimony of: (1) Mr. Stoddard; (2) Joseph E. Bowring, Manager of PJM's Market Monitoring Unit; and (3) Christine M. Schwab, Director of PJM Integration with Dominion Resources Services, Inc. Mr. Stoddard responds to the cost/benefit study submitted by the Staff and asserts that, compared to the overall cost of serving load during the study period, the estimated net benefits in DVP's cost/benefit study and in the Staff's cost/benefit study differ by only a few percentage points. Mr. Bowring responds to certain observations by Staff witness Spinner regarding the operation of PJM markets and the role of market monitoring. Mr. Bowring agrees that wholesale power markets require careful market monitoring, and he believes that an organized, centrally dispatched, security constrained, independently operated, transparent wholesale marketplace is superior to a standalone bilateral wholesale marketplace.

Ms. Schwab responds to the direct testimonies of Staff witness Walker, Consumer Counsel witness Brown, and Committee witness Dooley. Ms. Schwab agrees with Mr. Walker's recommended conditions, with certain clarifications and modifications. Ms. Schwab states that Mr. Brown's recommended condition numbers 2 and 3 regarding a single load zone and PJM's commitment not to shed load are acceptable with certain clarifications and modifications. Ms. Schwab testifies that the Company is unwilling to waive its rights under federal law to

change its transmission rate, as is suggested by Mr. Brown's condition number 4. Ms. Schwab states that Mr. Brown's first condition regarding an FTR "hold harmless" portfolio is unnecessary given capped rates and default service. Ms. Schwab rejects Consumer Counsel's remaining conditions, stating that they are unjust, unreasonable, contrary to state and/or federal law and would deny the Company rights to which it is entitled under state or federal law. In addition, Ms. Schwab asserts that Committee witness Dooley's recommendation to condition approval upon DVP foregoing, for retail ratemaking purposes, the deferral of PJM administrative costs is unjust, unreasonable, contrary to federal law and would deny the Company a right to which it is entitled under federal law.

On October 5, 2004, the FERC issued an Order Establishing PJM South, Subject to Conditions.[16] On October 6, 2004, DVP filed a Motion for Continuance with this Commission, wherein the Company requested that the public hearing scheduled for October 12, 2004, be retained to accept a stipulation or partial stipulation in this matter, but that the hearing otherwise be continued.

On October 12, 2004, prior to commencement of the public hearing, Virginia Power filed a Motion in Limine. The Motion in Limine requested that the Commission: (1) limit the testimony of Committee witness Dooley by ordering that his testimony and recommendation that the Company agree not to seek deferral of PJM administrative charges is not relevant to this proceeding; and (2) take notice of the Company's objection at the public hearing in accordance with controlling legal authorities by recognizing that Mr. Dooley's proposed condition dealing with FERC's authority over rate treatment and related accounting issues is not relevant to this proceeding.

[16] PJM South, Order Establishing PJM South, Subject to Conditions issued October 5, 2004 ("PJM South Order").

A public hearing was convened on October 12, 2004. At the hearing, the Commission received a Partial Stipulation executed by the following participants: DVP; the Staff; Consumer Counsel; PJM; Coral; Old Dominion Electric Cooperative; Chaparral (Virginia), Inc. ("Chaparral"); and the Municipal Electric Power Association of Virginia, Central Virginia Electric Cooperative, and Craig-Botetourt Electric Cooperative.[17] The Partial Stipulation recommends that the Commission accept the terms and conditions therein as conditions to any Order the Commission issues approving the Company's Application. The terms and conditions of the Partial Stipulation address, among other things: (1) certain reporting requirements for the Company, which shall cease with the filing of such reports in calendar year 2007 unless each Virginia incumbent electric utility that is a member of PJM as of September 30, 2007, is required to file reports containing substantially similar information after 2007; (2) certain reporting requirements for PJM, which shall end in 2010; (3) PJM's agreement to implement certain curtailment protocols designed to protect the Company's retail and wholesale customers for which DVP has a generation capacity obligation so long as DVP has maintained adequate generation capacity in accordance with applicable requirements; and (4) PJM's commitment to initiate a stakeholder process regarding any requests by load serving entities to change from a single load aggregation zone for the establishment of LMP pricing.

The Commission also received the testimony of one public witness at the hearing. The written statement of Irene E. Leech, President of the Virginia Citizens Consumer Council ("VCCC"), was read into the record and identified as Exhibit C. VCCC opposes DVP's proposal to join PJM and does not believe that it is the best option for consumers. VCCC believes that Virginia consumers will pay significantly higher prices for electricity if this transfer is approved.

[17] Exh. D. The Partial Stipulation is attached to this Order Granting Approval.

VCCC does not believe that the transfer is in the public interest and does not believe that the legislation passed by the Virginia General Assembly is too narrow to allow the public interest to be considered. VCCC states that allowing DVP to join PJM puts Virginia citizens' electric system at a significantly higher security risk. VCCC asserts that if FERC forces all states to join an RTO, there will be another RTO to our south, where electricity prices are much closer to historical Virginia prices and where the market will be more fair to consumers. VCCC contends that if the transfer is approved, there must be provisions that allow the Commission to force a change in RTO membership should conditions change, including the creation of another RTO that provides more public benefit. VCCC also states that taking this irrevocable step at this stage in the national process makes careful, conservative Virginia a guinea pig in the initial stages of a tremendously risky national experiment. VCCC asserts that, if the transfer is approved, the costs of PJM membership should be borne by DVP and its shareholders, not consumers who are being placed in a higher cost market with this move. VCCC states that, if the transfer is approved, there must be some way to protect consumers who buy their electricity from electric cooperatives or public power. VCCC asserts that, if the transfer is approved, there must be provisions to assure adequate, fully funded, irrevocable consumer representation in the PJM governance process. VCCC also states that the Commission should assure that it has the authority to hold the utility and PJM to fair service standards and quality for consumers over time – not just during a limited number of years. In sum, VCCC opposes the proposed transfer because it is only in the business interest, not the public interest.

Finally, during the October 12, 2004, hearing, the Commission also: (1) established a schedule for written responses to the Motion in Limine and for DVP's reply thereto; (2) granted

the Company's Motion for Continuance; and (3) scheduled the hearing to reconvene on October 25, 2004.

On October 19, 2004, responses in opposition to the Motion in Limine were filed by the Committee, Consumer Counsel, and the Staff. On October 21, 2004, DVP filed a reply to such responses.

The public evidentiary hearing was reconvened on October 25 and 26, 2004. James C. Roberts, Esquire, Edward L. Flippen, Esquire, and Michael C. Regulinski, Esquire, appeared on behalf of the Company. Judith Williams Jagdmann, Esquire, C. Meade Browder, Jr., Esquire, and D. Mathias Roussy, Jr., Esquire, appeared on behalf of Consumer Counsel. Louis R. Monacell, Esquire, and Edward L. Petrini, Esquire, appeared on behalf of the Committee. Donald J. Sipe, Esquire, appeared on behalf of MeadWestvaco Corporation ("MeadWestvaco"). Michael E. Kaufmann, Esquire, appeared on behalf of Chaparral. Thomas B. Nicholson, Esquire, appeared on behalf of Coral. Ralph L. Axselle, Jr., Esquire, Craig A. Glazer, Esquire, and Phillip T. Golden, Esquire, appeared on behalf of PJM. Mr. Urchie B. Ellis, Esquire, appeared pro se. William H. Chambliss, Esquire, Arlen K. Bolstad, Esquire, Glenn P. Richardson, Esquire, and Katherine A. Hart, Esquire, appeared on behalf of the Staff. After hearing oral argument on DVP's Motion in Limine, the Commission denied the motion. Thereafter, upon agreement of the participants, certain pre-filed testimony was accepted into the record without cross-examination. The remaining pre-filed testimony was accepted into the record subject to cross-examination.

NOW THE COMMISSION, having considered the record, the pleadings, and the applicable law, is of the opinion and finds as follows. We approve the Company's Application to

transfer functional and operational control of its transmission facilities to PJM, subject to the terms and conditions contained in the Partial Stipulation.

We recognize that there is testimony raising concerns over the integration of DVP into PJM. For example, those concerns include that: (1) PJM's LMP pricing could raise rates to Virginia ratepayers; (2) some customers may be adversely impacted by changes in how transmission costs are determined, allocated, and recovered; (3) any breakdown in communication within PJM could have significant implications for reliability; (4) market monitoring within PJM may not be effective; and (5) DVP's plan to defer RTO start-up costs and PJM administrative costs until the expiration of capped rates shifts the risk of cost increases during this period from shareholders to ratepayers.

Section 56-579 A 1 of the Restructuring Act, however, requires that an incumbent electric utility "shall transfer management and control of its transmission assets to a regional transmission entity by January 1, 2005, subject to Commission approval as provided in this section" (emphasis added). Accordingly, it is the policy of this Commonwealth, as directed by the General Assembly, that incumbent electric utilities shall transfer management and control of transmission assets to an RTE by New Year's Day 2005. In this regard, we agree with Staff witness Walker that PJM represents one of the best, if not the best, available RTE models and is the only feasible option at this time for DVP to satisfy the requirements of the Restructuring Act.

In addition, § 56-579 F of the Restructuring Act provides as follows:

> Any request to the Commission for approval of such transfer of ownership or control of or responsibility for transmission facilities shall include a study of the comparative costs and benefits thereof, which study shall analyze the economic effects of the transfer on consumers, including the effects of transmission congestion costs. The Commission may approve such a transfer if it finds, after notice and hearing, that the transfer satisfies the conditions contained in this section.

This statute does not include an express standard upon which the Commission is to approve or to disapprove the Application based on the results of a cost/benefit study. The statute does not make a positive net benefit finding a prerequisite for approval of the Application. Rather, there may be some implication that the Commission should reject the Application if the cost/benefit study shows a significant detriment. In contrast, the Restructuring Act includes an express requirement that incumbent electric utilities transfer management and control of transmission assets to an RTE by January 1, 2005, subject to Commission approval. Va. Code § 56-579 A 1. The Company submitted a cost/benefit study pursuant to this statute, and the Staff also filed a cost/benefit study. The Company's cost/benefit study estimates that integration into PJM will result in net benefits. The Staff's cost/benefit study produces a slight net benefit if it is assumed that DVP does not recover deferred PJM administrative costs after the expiration of capped rates. If DVP recovers such deferred costs after capped rates expire, the Staff's results range from a slight net cost to a slight net benefit. In any event, the range of net costs and benefits produced by the Staff's cost/benefit study is only a few percentage points of the Company's total costs of serving load. Accordingly, we find that the cost/benefit studies do not establish a significant economic detriment.

Committee witness Dooley recommends that the Commission condition any approval in this case on Virginia Power agreeing not to seek FERC's approval to defer PJM administrative charges for retail ratemaking purposes.[18] The Company argues that this Commission does not

[18] Mr. Dooley also states that DVP has not requested similar deferred accounting treatment for its retail customers in North Carolina, and he concludes that this creates an inequity for Virginia consumers. However, as recognized by FERC in its recent order on PJM South, North Carolina has not implemented a retail open access program. PJM South Order at 4, n.14. Thus, the Company explains that it is not asking for deferred accounting for customers in North Carolina because – unlike Virginia – retail rates in North Carolina have not been unbundled. See, e.g., Tr. at 494; PJM South, Joint Application to Establish PJM South at 17, n.36. Indeed, we note that the Commission's Addendum to 2002 Status Report on Competition, dated January 3, 2003, and presented to the Governor and General Assembly, recommended that retail rates be re-bundled in Virginia. This recommendation was not

have the authority to require such a condition. The Company states that it has requested FERC approval to defer such costs for accounting purposes, and that FERC has exclusive jurisdiction over the accounting and ratemaking treatment of these transmission-related costs. The Committee counters, however, that no FERC order prevents the Commission from imposing Mr. Dooley's recommended condition, and that DVP cites no authority to that effect.

In this regard, we agree with the Staff's explanation that the resolution of FERC's accounting and ratemaking treatment of PJM administrative charges properly lies with the FERC. Staff further notes that Virginia Power may seek FERC's approval for recovery of such charges through a future filing with FERC under Section 205 of the FPA, or that FERC could perhaps determine its ratemaking treatment of such charges through a proceeding under Section 206 of the FPA initiated by complaint or by FERC's own motion. We will not adopt Mr. Dooley's recommendation, which would require the Company not to pursue rights that it may possess under federal law. We agree with the Staff that FERC's accounting and ratemaking treatment of these charges remains an open question. Likewise, this Commission's treatment of such charges also remains an open question. This Commission has the authority to prescribe how the Company maintains its books and records for Virginia jurisdictional purposes. In addition, as noted during the hearing, the Commission has approved the Company's tariffs for the unbundled transmission component of capped retail rates. The Company has not sought, and the Commission has not granted, authority to treat any RTO start-up or PJM administrative charges as a deferred regulatory asset. Accordingly, DVP must continue to expense these charges for Virginia jurisdictional purposes unless it seeks and obtains approval from this Commission to treat such charges otherwise.

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implemented, so that the Company is correct that Virginia's retail rates remain unbundled. Mr. Dooley's comparison between North Carolina and Virginia is not apposite.

Further in this regard, MeadWestvaco argued at the hearing that, if FERC permits DVP to defer PJM administrative charges and to recover such after the expiration of capped rates, this Commission may take into account the Company's earnings under capped rates and credit such earnings against payment of the deferred charges.[19] MeadWestvaco asserted that the only thing this Commission must assure, to pass constitutional muster, is that over a reasonable period of time – and such time being within the Commission's discretion to determine – DVP has a reasonable opportunity to recover any FERC-approved costs.[20] If MeadWestvaco is correct, then the condition recommended by Mr. Dooley is unnecessary because this Commission, at a later date, may determine whether any deferred PJM administrative charges already have been recovered in retail rates over a reasonable period of time. We do not, however, reach these questions. As pointed out by Virginia Power, this is not a ratemaking proceeding.

Next, we note that both Mr. Ellis and Ms. Leech oppose the Company's application as contrary to the public interest. However, § 56-579 of the Restructuring Act – unlike other provisions of Title 56 of the Code – does not explicitly provide the Commission with a general grant of broad discretion to find that any such transfer is in the public interest. Rather, § 56-579 A 2 directs the Commission to develop rules and regulations under which the incumbent electric utility may transfer control, ownership, or responsibility of transmission capacity to an RTE, upon such terms and conditions that the Commission determines will, among other things, "[g]enerally promote the public interest." As discussed above, the Commission developed the

[19] MeadWestvaco cited the following cases for this proposition: Monongahela Power Company v. Schriber, 322 F.Supp.2d 902 (S.D. Ohio 2004); and Pacific Gas and Electric Company v. Lynch, 216 F.Supp.2d 1016 (N.D. Cal. 2002) ("Pacific Gas").

[20] MeadWestvaco argued that in Pacific Gas: (1) the state public utility commission did not increase the retail rate to reflect an increase in the wholesale rate; and (2) the court found that the filed rate doctrine is not violated if, after looking at past over-recoveries by the utility, the state public utility commission finds that there was not an undercollection of FERC-approved costs over a reasonable period of time.

RTE Rules as required by this statute; the RTE Rules establish elements of an RTE structure essential to the public interest. The RTE Rules require the examination of, for example, an RTE's reliability practices, pricing and access policies, and independent governance. We agree with Staff witness Walker that the Company's request to join PJM sufficiently satisfies the RTE Rules.

In sum, we find that the Company's request to transfer functional and operational control of its transmission facilities to PJM, subject to the terms and conditions contained in the Partial Stipulation, satisfies the RTE Rules and the directives set forth in the Restructuring Act. Accordingly, based on the evidence in this case and the Partial Stipulation, we find that the Restructuring Act requires our approval of the Application.

Accordingly, IT IS ORDERED THAT:

(1) Virginia Power's Application to transfer functional and operational control of its transmission facilities to PJM is hereby approved, subject to the terms and conditions contained in the Partial Stipulation.

(2) The Partial Stipulation is made part of this Order Granting Approval, and the parties thereto shall comply with its provisions.

(3) This case is continued generally.

AN ATTESTED COPY hereof shall be sent by the Clerk of the Commission to all persons on the official Service List in this matter. The Service List is available from the Clerk of the State Corporation Commission, c/o Document Control Center, 1300 East Main Street, First Floor, Tyler Building, Richmond, Virginia 23219.